STATE OF CALIFORNIA

STATE BOARD OF EQUALIZATION

PROPERTY AND SPECIAL TAXES DEPARTMENT
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October 4, 2011

Dear Interested Party,

Attached is a copy of Special Taxes and Fees Current Legal Digest (CLD) Number 2011-1 for your information and review. This CLD contains new annotations, proposed revisions to existing annotations and deletions of annotations that no longer represent the opinion of the Board of Equalization's (Board) legal staff. After reviewing, please submit any questions, comments, or suggestions for changes by November 3, 2011. You may complete the electronic CLD Comments Form at http://www.boe.ca.gov/sptaxprog/cld_comments.htm , or mail your written comments to:

Board of Equalization
Special Taxes and Fees Annotation Coordinator, MIC: 57
P.O. Box 942879
Sacramento CA 94279-0057

Please note, the new annotations and/or suggested revisions of existing annotations contained in the attached CLD are drafts and may not accurately reflect the Board's official position on certain issues nor reflect the language that will be used in the final annotation.

CLDs are circulated for 30 days, at which time any questions are addressed and/or suggested modifications taken into consideration. After review of the final version by the Board's Legal Division, they are printed in Volumes 3 and 4 of the *Business Taxes Law Guide*. At that time, the CLD becomes obsolete.

If you have any questions, please contact Robert Zivkovich at 916-324-2775.

David J. Gau,
Deputy Director
Property and Special Taxes Department

DJG: rz

Enclosures: Special Taxes and Fees Current Legal Digest 2011-1
Redacted Legal Opinions Related to Emergency Telephone Users Surcharge and Energy Resources Surcharge

SPECIAL TAXES CURRENT LEGAL DIGEST NO. 2011-1

October 4, 2011

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SPECIAL TAXES AND FEES ANNOTATIONS

DIESEL FUEL TAX

Delete Annotation and Heading.

QUALIFIED HIGHWAY VEHICLE OPERATOR

Vehicles Registered with DMV as "Special Equipment."

~~An operator of a street sweeper vehicle that is registered with the California Department of Motor Vehicles as "special construction equipment" (i.e., has a "SE" license plate), which is only incidentally operated or moved on the public highways, may apply to the Board for a license as a "qualified highway vehicle operator," pursuant to sections 60027 and 60161, and purchase dyed diesel fuel for use in the street sweeper vehicle. However, the operator must report and pay to the Board the backup tax on untaxed dyed diesel fuel that is used while operating or moving the diesel-powered street sweeper vehicle on a highway, pursuant to section 60058. 9/05/06.~~

Delete annotation - Several years ago, the IRS reversed how it administered the use of dyed diesel fuel in certain vehicles deemed to be special equipment. Previously, the Fuel Taxes Division (now the Special Taxes and Fees Division) had a program allowing qualified highway vehicle operators of special equipment that used dyed fuel on the highway to pay the diesel fuel tax directly to the Board of Equalization (BOE), but the program was cancelled in order to be consistent with the IRS ruling. Operators of special equipment are no longer allowed to use dyed fuel on the highways in California. Taxpayers were advised that the BOE was suspending the program in the December 2008 Fuel Taxes Newsletter, page 3 (http://www.boe.ca.gov/lawguides/business/current/btlg/vol3/dfta/dfta-8.html).

EMERGENCY TELEPHONE USERS SURCHARGE

Federal Universal Service Fund Charge

The federal government requires service suppliers to contribute to the Federal Universal Service Fund (FUSF), and service suppliers may pass on, if they choose, the cost of this contribution to their customers, which they do in the form of a line item called a variety of different names (e.g., "Federal Universal Service Fee" or "Universal Connectivity Fee"). Regardless of the name by which it is called, if the charge is for recoupment of the

cost of the service supplier's contribution to the FUSF, the charge is not subject to the Emergency Telephone Users Surcharge. 1/8/10.

Add Annotation- As a result of a Board of Equalization decision in December 2006 and a California Superior Court's rulings (*Sprint Communications Co., L.P. v. State Bd. of Equalization* (Super. Ct. S.F. County, 2009, No. CGC-06-455982), with which the Board chose to acquiesce.

California Public Utilities Commission Mandated Charges

The California Public Utilities Commission mandates the imposition of a number of charges and surcharges on service suppliers and service users, some of which are subject to the Emergency Telephone Users (911) Surcharge and some of which are not. The charges that are subject to the 911 Surcharge are: the California Public Utilities Commission Reimbursement (or PUC) Fee and the California Relay Service and Communications Devices Fund (CA Relay SVC/Comm) Surcharge. The charges that are not subject to the 911 Surcharge are: the Universal LifeLine Telephone Service (ULTS) Surcharge; the High-Cost Fund-A and Fund-B Surcharges; and the California Teleconnect Fund (CTF) Surcharge. 1/8/10.

Add Annotation- As a result of a Board of Equalization decision in December 2006 and a California Superior Court's rulings (*Sprint Communications Co., L.P. v. State Bd. of Equalization* (Super. Ct. S.F. County, 2009, No. CGC-06-455982), with which the Board chose to acquiesce.

Proration of Flat Rate Service Charges or Monthly Recurring Charges

Since flat rate service charges, also known generally as monthly recurring charges, are both intrastate and interstate in nature, they must be prorated to determine the intrastate portion of the total charge, and the Emergency Telephone Users (911) Surcharge should only be applied to the intrastate portion. Of the two types of monthly recurring charges that must be prorated to determine the amount of their intrastate component, the first is flat rate charges (variously named) that the service supplier bills, generally in connection with its various calling plans, to its customers, the service users, each billing period and that do not vary based on the number, length, or time elapsed of any toll calls made during the billing period. The second type is charges (also variously named) that are intended to reimburse the service supplier for amounts it pays to local telephone companies for access to and use of local telephone lines so that its customers can make intrastate, interstate, and international long distance phone calls. Both types of charges:

- Are billed by service suppliers as part of their various billing plans and must be paid by their customers as a precondition to the customer being able to make long distance calls, whether intrastate, interstate, or international.
- Are billed to a customer in the exact same amount each month, whether or not the customer makes any long distance calls during the billing period and whether or not

Please note that the new proposed annotation contained in this CLD is a draft and may not accurately reflect the text of the final annotation

all long distance calls made during the billing period are intrastate or interstate or some combination of each. .

- Are set forth in the service supplier's federal tariffs, filed with the Federal Communications Commission, not with the California Public Utilities Commission.

However, monthly recurring flat charges that have been historically associated with the provision of local telephone service are not subject to proration. In addition, the flat charge made by service suppliers for recoupment of their contribution to the Federal Universal Service Fund should not be prorated because it does not have an intrastate component and is not subject to the 911 Surcharge. 1/8/10.

Add Annotation- As a result of a Board of Equalization decision in December 2006 and a California Superior Court's rulings (*Sprint Communications Co., L.P. v. State Bd. of Equalization* (Super. Ct. S.F. County, 2009, No. CGC-06-455982), with which the Board chose to acquiesce.

Proration of Flat Rate Service Charge

~~Recurring flat rate service charges are subject to the Emergency Telephone Users Surcharge without proration by intrastate and interstate calls. 12/28/93.~~

Delete Annotation - The decision in *Sprint Communications Co., L.P. v. State Bd. of Equalization* (Super. Ct. S.F. County, 2009, No. CGC-06-455982) ruled that flat rate service charges that have both intrastate and interstate components must be prorated and that the Emergency Telephone Users Surcharge must only be applied to the intrastate portion.

PUC Fee

~~The PUC fee and the Universal Telephone Service Tax (Moore Tax) are subject to the surcharge. 6/17/91.~~

Delete Annotation - The Universal Service Tax (Moore Tax), imposed pursuant to the former Revenue and Taxation Code section 44030, no longer exists and has not existed for a number of years. In addition, what constitutes the "PUC fee," and application of the Emergency Telephone Users Surcharge to the fee, is more clearly described in the new annotation proposed above.

Subscription Fees

~~Subscription fees, which are monthly flat rate administrative fees imposed on users by the service carrier regardless of whether any calls are made by the customer, are mandatory charges imposed as a condition precedent to obtaining intrastate as well as interstate long distance services and are subject to the surcharge. 10/09/92.~~

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Delete Annotation - The decision in *Sprint Communications Co., L.P. v. State Bd. of Equalization* (Super. Ct. S.F. County, 2009, No. CGC-06-455982) ruled that flat rate service charges that have both intrastate and interstate components must be prorated and that the Emergency Telephone Users Surcharge must only be applied to the intrastate portion.

Universal Telephone Service Surcharge

~~The Universal Telephone Service surcharge administered by the PUC is a state tax and is not excluded from the charges for services upon which the Emergency Telephone Users Surcharge is based. 4/20/88.~~

Delete Annotation - Based on its Web site and other sources, it is apparent that the California Public Utilities Commission no longer administers a surcharge that is called the "Universal Telephone Service" surcharge. Moreover, to the extent that it may have been the precursor of the Universal LifeLine Telephone Service (ULTS) Surcharge, it would not be subject to the Emergency Telephone Users Surcharge, based on the decision in *Sprint Communications Co., L.P. v. State Bd. of Equalization* (Super. Ct. S.F. County, 2009, No. CGC-06-455982).

ENERGY RESOURCES SURCHARGE

CO-GENERATION BY CUSTOMERS

Net Energy Metering.

Under the Public Utilities Code, "net energy metering" involves "measuring the difference between the electricity supplied through the electric grid and the electricity generated by an eligible customer-generator and fed back to the electric grid over a 12-month period" and means using a single meter capable of registering the flow of electricity in two directions, so that the customer is accurately billed or credited. Such customers may be net surplus generators or net consumers. The Energy Resources Surcharge is imposed on the consumption of electrical energy purchased from an electric utility, and every person consuming electrical energy in this state purchased from an electric utility is liable for the surcharge. The fact that the customer also generates electricity does not alter the fact that the customer has consumed electricity purchased from (i.e., supplied by) an electric utility. Furthermore, the amount of electricity consumed by the customer is offset by the amount of the electricity generated by the customer and fed back to the electric grid. Hence, the electricity generated by the customer is a form of consideration "paid" by the customer to the electric utility in exchange for the electricity the customer consumed.

Accordingly, the surcharge must be applied to the total amount of electricity supplied by the utility and consumed by the customer, and whether the customer is a "net consumer" or a "net generator" does not affect how the surcharge is applied. 6/7/11.

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State of California

Board of Equalization
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Memorandum

CONFIDENTIAL: ATTORNEY-CLIENT PRIVILEGE

To: Ms. Lynn Bartolo, Chief
Excise Taxes Division (MIC:56)

Date: January 8, 2010

From: Carolee D. Johnstone
Tax Counsel III (Specialist)
Tax and Fee Programs Division (MIC:82)

Subject: APPLICATION OF THE EMERGENCY TELEPHONE USERS SURCHARGE LAW FOLLOWING RECENT SUPERIOR COURT AND BOARD DECISIONS
Assignment No. 09-426

You have asked for guidance with respect to how the Excise Taxes Division (ETD) of the Board of Equalization (Board) should proceed in applying the Emergency Telephone Users (911) Surcharge Law following recent decisions by the California Superior Court, County of San Francisco, and the Board. Each of the charges at issue on which the court and the Board decided in favor of Sprint Communications Company, L.P. (Sprint) and Qwest Communications Corporation (Qwest) are discussed in detail below.[1]

A. BACKGROUND

The principal source of the matters at issue here is the judgment that was entered on October 26, 2009, in *Sprint Communications Company, L.P. v. State Bd. of Equalization* (Super. Ct. S.F. County, 2009, No. CGC-06-455982) (*Sprint*), in favor, in large part, of Sprint, based on the court's Decision After Nonjury Trial (filed February 18, 2009) (Decision), Order Amending the February 18, 2009 Decision After Nonjury Trial (filed April 17, 2009) (Order Amending Decision), and Order Regarding Methodology for Calculating Refund Due to Sprint (filed August 20, 2009) (Order Regarding Methodology) (collectively, *Sprint* decision). This judgment was served on the Board on November 3, 2009, and will be final on January 2, 2010. In addition, on December 12, 2006, the Board decided several issues in the *Qwest Communications Corporation* (*Qwest*) appeal. As a result of both of these decisions, a number of questions have come up with respect to program implementation and application of the 911 surcharge to certain charges made by telephone communication service suppliers, the taxpayers. Each of these questions is addressed below.

[1] The Court found in favor of the Board with respect to the proper way to calculate the sum of the surcharge on a bill, pursuant to Revenue and Taxation Code section 41025, so this issue will not be discussed here. On the other hand, although the Board adopted the staff recommendation with respect to the Access Line Charge billed by Qwest (i.e., that it was intrastate in nature and, therefore, subject to the surcharge according to the long standing Board position), it appears, as discussed below, that the court ruling regarding monthly recurring charges would affect the Board's decision regarding the Access Line Charge, in that, although that flat charge did have an intrastate component, it may need to be prorated based on intrastate and interstate usage.

B. PROGRAM IMPLEMENTATION

1. What application, if any, does the *Sprint* decision have beyond Sprint itself and the audit period at issue in that case?

Under the state Constitution, the Board is prohibited from declaring a statute unconstitutional and from declaring a statute unenforceable or refusing to enforce a statute unless an appellate court has determined that the statute is unconstitutional. (Cal. Const., art. III, § 3.5, subds. (a) & (b).) Otherwise, the Board is delegated broad power, authority, and discretion to interpret, enforce, and implement the tax laws it administers and to adopt, amend, and repeal regulations, in accordance with the requirements of the Administrative Procedure Act (APA). (Gov. Code, § 11340 et seq.) Specifically, the Board has the power, authority, and discretion to administer the 911 Surcharge Law with respect to imposition of the 911 surcharge: "The board shall enforce the provisions of this part and may prescribe, adopt, and enforce rules and regulations relating to the administration and enforcement of this part." (Rev. & Tax. Code, § 41128.)[2]

The Board's expertise in administering the 911 Surcharge Law and its reliance on the court's rulings in *Sprint*, combined with the authority granted to the Board in section 41128, give the Board the authority to acquiesce to adverse trial court opinions, if warranted. Further, it is our opinion that such acquiescence would extend to application of the court's rulings not only to other Sprint audit periods but also to the industry as a whole – in other words, the court's rulings, as implemented by the ETD, would become part of the general administration of the 911 surcharge program.

However, whether acquiescence to the trial court's rulings is warranted is not so much a legal question as it is a practical one. Subject to certain qualifications discussed below, we advise in favor of acquiescence for the following reasons. First, it is unlikely that, with respect to most, if not all, of the court's rulings, the outcome would be any different in further litigation, and the Board has already decided, in *Qwest*, that the Universal Service Fund Charge (or Federal Universal Service Charge, as Sprint called it) is not subject to the surcharge. Second, the Board has decided not to appeal these legal issues. Third, it is evident that the *Sprint* case has already caused significant disruption in ETD's normal audit and petition process, and it would make sense to bring the disputes regarding the charges at issue to a conclusion so that ETD can resume its normal process.

Further, with respect to the "time-only" charges (the "and/or" issue), the 2008 legislation has made the time for raising the dispute regarding these charges finite – the dispute is not relevant as of May 21, 2008. Thus, we further advise ETD to resolve expeditiously the cases that involve such charges, both those pending and any additional claims for refund that are submitted prior to the running of the statute of limitations, i.e., three years from the last day of the second month following the date on which the overpayment was made on surcharge amounts billed prior to May 21, 2008. (§ 41101.)

In addition, although the court's ruling that monthly recurring flat charges that are both intrastate and interstate in nature must be prorated based on usage goes against the Board's general historical position, the 2008 legislation expressly authorizes service suppliers to prorate certain charges. Thus, acquiescence to the court's ruling regarding proration would be appropriate and consistent with current law.

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[2] All future statutory references will be to the Revenue and Taxation Code unless stated otherwise.

2. Does the *Sprint* decision apply only to "wireline" services?

While the "case only concerns 'wireline' telephone services," and not wireless or cellular telephone services, the court's rulings are not necessarily applicable only to "wireline" telephone services. (See Decision, *supra*, at p. 3 [emphasis added].) Since the court's rulings involve interpretations of various provisions of the 911 Surcharge Law, which are applicable to all forms of telecommunication services, not just wireline services, it is reasonable to conclude that the rulings should also be applied to all forms of telecommunication services. Accordingly, it is our opinion that the Board has the authority, as described above, to apply the court's rulings to all means by which telephone communication services are delivered, and we advise ETD to do so.

3. How should the *Sprint* decision be applied to pending audits and petitioned audit liabilities that have been held in abeyance pending the outcome of the *Sprint* case?

Subject to the qualifications discussed below, based on the foregoing, the rulings from the *Sprint* and *Qwest* decisions should be applied to pending audits and petitioned audit liabilities for those charges that are relevant to each audit and liability.

4. How should the *Sprint* and *Qwest* decisions be applied to pending claims for refund submitted by service suppliers and by service users that involve issues decided in these cases? Is there a difference?

As indicated in 3, above, the rulings from the *Sprint* and *Qwest* decisions should be applied to pending claims for refund, depending on the charges involved, as discussed below. However, application of the decisions to claims for refund from service suppliers does differ from application of the decisions to claims for refund from service users.

For service suppliers, the key will be whether the claim is for surcharge amounts paid to the Board after the amounts were collected from service users or the claim is for surcharge amounts paid to the Board as a result of a determination issued by the Board. If the surcharge amounts were collected from service users, the service supplier does not have standing to claim a refund of those amounts unless it can show that it has refunded the amounts to the service users. (§ 41100.) If the service supplier paid the surcharge amounts because of a determination issued by the Board and the service supplier can show that these amounts were not collected from service users, then the service supplier may be eligible for a refund, depending on the specific charges involved, as discussed below.

For service users, the key will be whether they can show that the surcharge amounts they paid resulted from application of the surcharge to the charges that are affected by the decisions and not from other charges. For example, while toll charges that did not vary by time and distance would not be subject to the surcharge prior to May 21, 2008, toll charges that did vary by time and distance would be subject to the surcharge. They would also have to show that the surcharge was applied to, e.g., the appropriate CPUC-mandated charges by the service supplier in order to support the amount of refund to which they claim they are entitled. They would also have to show that, with respect to any monthly recurring charges or flat rate charges, the service supplier applied the surcharge to the full amount of these charges (i.e., not a prorated amount).

5. Going forward, what is the effective date, if there is one, for implementing the changes mandated by the *Sprint* and *Qwest* decisions?

The judgment in *Sprint* was filed on October 26, 2009, and will be final on January 2, 2010. The Board's decision in *Qwest* was made on December 12, 2006. Neither the court nor the Board provided any express guidance as to when their rulings should be considered to be in effect, either retroactively or prospectively. However, in both decisions, the rulings were meant to make clear that the charges at issue were never meant to have been subject to the surcharge or, with respect to the monthly recurring charges, that they should have always been prorated. Consequently, there is no set effective date for implementing the court's and Board's rulings since they are, essentially, already effective.

On the other hand, practically speaking, it would be helpful for the ETD to establish an operative date in order to efficiently administer the 911 surcharge program (i.e., a date on and after which service suppliers would be advised to stop collecting the surcharge on certain charges and start prorating flat charges that are both intrastate and interstate in nature, similar to the monthly recurring charges at issue in *Sprint*). It is suggested that a date be chosen far enough in the future to allow for adequate notification and for the service suppliers to adjust their billing programs to accommodate the changes. Depending on when a notice can be issued (see 6, below), it is suggested that an operative date be set using terms from the statutes, something to the effect that: "No service suppliers of intrastate telephone communication and Voice over Internet Protocol (VoIP) services shall apply the Emergency Telephone Users (911) Surcharge to the following charges billed by the service supplier to the service user on and after [Month] 1, 2010[3]: the federal Universal Service Fund charge and the California Universal LifeLine Telephone Service surcharge, High-Cost Fund-A and Fund-B surcharges, and California Teleconnect Fund surcharge.

For 911 surcharge amounts improperly collected (based on the court and Board rulings) by service suppliers on bills issued prior to the chosen operative date, service users may submit claims for refund for any excess surcharge amounts they can establish they paid.

6. Should the Board notify service suppliers of the *Sprint* decision and the resulting changes in how they are to bill and collect the 911 surcharge? If yes, when should this notification be issued, and what information should it contain?

We advise that the Board should notify service suppliers of the rulings made in the *Sprint* decision and to provide an explanation of the charges affected. As noted above, this notification should be sent out as soon as possible after the judgment is final on January 2, 2010. The notice should, at a minimum: (1) provide a short explanation of the *Sprint* case; (2) provide detailed descriptions of each of the charges affected and how calculation of the 911 surcharge amount will be affected (per below); and (3) provide the chosen operative date (see 5, above).

[3] This date that should be at least 47 days after the notice is issued. (See §§ 41032 [providing that notice shall be mailed "no later than November 15" advising service suppliers of the new rate to be effective January 1 (i.e., 47 days of advance notice)], 41050 [the surcharge "attaches at the time charges for . . . services . . . are billed by the service supplier to the service user"]).

7. Should the Board notify service users of their eligibility to claim a refund of the 911 surcharge that may have been improperly collected from them?

While the Board has no legal obligation to notify service users of the effect if the *Sprint* and *Qwest* decisions and how claims for refund may be filed and substantiated, we advise that ETD promptly enlist the expertise of the Board's External Affairs Department for ideas on how to disseminate such a notice, including, but not limited to: press releases; Web site postings; and articles in sales and use tax TIBs and other tax and fee bulletins.

8. How should the *Sprint* and *Qwest* decisions be applied to future claims for refund submitted by service suppliers and by service users that involve issues decided in these cases? Is there a difference?

See the discussion in 7, above, and the discussions below regarding how the various charges and calculation of the surcharge imposed on them are affected. The differences in future claims for refund from service suppliers and those from services users are the same as the differences described in 4, above.

C. SPECIFIC CHARGES AFFECTED BY THE *SPRINT AND QWEST* DECISIONS

1. Universal Service Fund Charge

As noted above, in December 2006, the Board decided that the Universal Service Fund Charge that Qwest billed its customers was not subject to the 911 surcharge, and the Board conceded this issue in the *Sprint* case, before the court was asked to rule on it. Based on the Board's decision, the 911 surcharge should not have ever been imposed on the Universal Service Fund Charge, the Federal Universal Service Charge (as Sprint calls it), or any other similar charge by any other name (collectively, USF charge). Accordingly:

- With respect to pending audits, if the service supplier did not include the USF charge when it calculated the surcharge it billed its service users, no action is necessary unless the auditor has already included the surcharge on the USF charge when he/she calculated the additional surcharge amount due (in which case, the surcharge on the USF charge must be backed out). At the same time, if the service supplier did include the USF charge when it calculated the 911 surcharge it billed its service users, again, no action is necessary, assuming (1) the service supplier collected the surcharge on the USF charge and remitted it to the Board and (2) the service supplier is unable or unwilling to refund the excess amounts to the service users who paid them. Under such circumstances, the service supplier is not eligible for a refund of, or credit for, the excess surcharge amounts. (§ 41100.)

- The same would apply to petitioned audit liabilities.

- With respect to both pending and future claims for refund from service suppliers, if the service supplier paid the surcharge on the USF charge as a result of a determination issued by the Board and did not collect the surcharge on the USF charge from its service users, the service supplier would be entitled to a refund of the excess surcharge amounts paid for

all open periods. However, as discussed above, service suppliers are not entitled to a refund of 911 surcharge amounts on USF charges they collected from their service users because service suppliers do not have standing to claim a refund of surcharge amounts they collected unless they can show they refunded those amounts to the service users.

- With respect to both pending and future claims for refund from service users, if the service user can show that the service supplier included the USF charge when it calculated the 911 surcharge amount billed and if the claim is within the three-year statute of limitations, the service user would be entitled to a refund of the 911 surcharge amounts it paid on the USF charge.

2. California Public Utilities Commission (CPUC)-Mandated Charges

The only CPUC-mandated charges that are affected by the *Sprint* decision are: the Universal LifeLine Telephone Service (ULTS) surcharge; the High-Cost Fund-A and Fund-B surcharges; and the California Teleconnect Fund (CTF) surcharge. The California Public Utilities Commission Reimbursement (PUC) Fee was never at issue in the litigation (i.e., not included in Sprint's complaint or trial brief), and Sprint withdrew its arguments regarding the California Relay Service and Communications Devices Fund (CA Relay SVC/Comm) surcharge. (Decision, *supra*, at pp. 16:6-25, 17:1-11.) The analysis provided above for the USF charge would also apply to the ULTS, High-Cost Fund-A and Fund-B, and CTC surcharges.

Service suppliers should continue to apply the 911 surcharge to the PUC Fee and the CA Relay SVC/Comm surcharge when calculating the 911 surcharge amounts to be billed and, if the service suppliers have not been collecting the 911 surcharge on these charges, the ETD should include the appropriate amounts in the amount of additional surcharge owed as a result of an audit.

3. Monthly Recurring Charges (MRCs), including the Presubscribed Line Charge

Sprint claimed that its Presubscribed Line Charge (PLC), its flat-rate service charges, and its flat-rate fees were not subject to the 911 surcharge because they were solely interstate in nature. (Complaint for Refund of Tax, 2/9/07, at ¶¶ 9 & 11.) The Board argued that these charges had an intrastate component and, based on section 41025 and long standing Board opinions, the charges were therefore subject to the 911 surcharge, without any proration. The court agreed with the Board that these charges, all of which it designated as "monthly recurring charges" (MRCs), did have an intrastate component, but ruled, contrary to the Board's position, that the MRCs should be prorated, based on usage, and that the 911 surcharge should be imposed only on the intrastate portion of the charge. (Decision, *supra*, at pp. 5-12.)

The first question is, since other service supplier's call charges are similar to Sprint's MRCs but are generally called by different names, what types of charges does the court's ruling apply to and what types does it not apply to? To begin, the ruling would not apply to monthly recurring flat charges that have historically been associated with the provision of local telephone service. (§§ 41011, subd. (a), 41015, subd. (b).)

There are two types of monthly recurring charges to which the court's ruling would apply. The first type are flat rate charges that the service supplier bills, generally in connection with its various calling plans, to its customers, the service users, each billing period and that do not vary based on the number,

length, or time elapsed of any toll calls made during the billing period. The second type are charges (i.e., the PLC) that are intended to reimburse the service supplier for amounts it pays to local telephone companies for access to and use of local telephone lines so that its customers can make intrastate, interstate, and international long distance phone calls. (See Decision, *supra*, at p. 5:7-12.) The factors common to both types of charges are:

- Both are imposed by service suppliers as part of their various billing plans and must be paid by their customers as a precondition for the customer to be able to make long distance calls at all, whether intrastate, interstate, or international. (*Id.* at p. 5:12-16.)

- Both types of charges are billed to a customer in the exact same amount each month, "whether or not the customer makes any long distance calls during a billing period and whether or not all long distance calls made during the billing period are intrastate or interstate or some combination of each." (*Id.* at p. 5:17-21.)

- Both types of charges are set forth in the service supplier's federal tariffs, filed with the Federal Communications Commission, not with the CPUC. (*Id.* at p. 5:21-23.)

Examples of the first type of MRCs would be the "monthly recurring charges" Sprint required customers to pay who signed up for Sprint Sense AnyTime (Tariff F.C.C. No. 1, at p. 186.266 [$4.95 as of 5/29/99]) and Business Sense (Tariff F.C.C. No. 11, at p. 142.22 [monthly service charge of $7.50 (as of 12/3/98) if the customer's monthly usage was less than $15.00]). An example of the second type would be Qwest's "Access Line Charge," which was Qwest's method of recouping the cost of the Presubscribed Interexchange Carrier Charge (PICC) it paid to local exchange carriers for access to a local telephone system so that it could provide long distance service to its customers. The Access Line Charge was imposed for the same reason as was Sprint's PLC and meets all three criteria and would, therefore, be a MRC covered by the ruling.

Any flat rate charge, other than a "USF" flat charge or those associated with local telephone service, that is billed monthly and meets the three criteria set forth above, is subject to imposition of the 911 surcharge on the intrastate portion of the charge, as determined.

The second question is, how should a service supplier calculate the intrastate state portion of these charges? After considerable discussion, the court agreed with the Board's suggested approach and ruled that the intrastate portion of Sprint's MRCs on all bills at issue, whether they included long distance call charges or not, should be determined by "summing, separately, all of the intrastate and interstate call charges on those bills that include long distance call charges, and calculating the percent of intrastate calls charges versus interstate call charges." (Order Amending Decision, *supra*, at pp. 2:30, 3:1-2.) The resulting intrastate percentage should then be applied to the MRCs on all of the bills. (*Id.* at p. 3:3-5.)

This method, expanded to billings for either a service supplier's entire customer base in California or broken down for California customers who subscribe to particular plans it offers, is similar to two of the methods permitted for determining the interstate portion of charges under section 41020: by books and records kept in the regular course of business (subd. (b)(1)(A)); and by traffic and call pattern studies representative of, here, how the service supplier chooses to group its California customers. In short, the court's ruling on the method by which the intrastate portion of Sprint's MRCs should be calculated is applicable to "MRCs" billed by other service suppliers.

Due to the complexities associated with such proration, it is strongly suggested that ETD initiate an interested parties process that would result in the promulgation of a regulation describing appropriate proration method(s). This regulation should also codify the other significant aspects of the *Sprint* and *Qwest* decisions discussed herein, including the incorporation of the chosen operative date. I would be happy to assist ETD in this rulemaking endeavor.

4. "Time-Only" Charges – the "And/Or" Issue

Again after considerable discussion, the court ruled that the "and" in subdivision (a)(1) of section 41016, as it then read – that "toll telephone service" meant "[a] telephonic quality communication for which . . . there is a toll charge which varies in amount with the distance and elapsed transmission time of each individual communication" (§ 41016, subd. (a)(1) [emphasis added]) – meant "and," not "or." (Decision, *supra*, at pp. 14:13-25, 15:1-19.) Therefore, the 911 surcharge that was collected on all long distance charges that did not vary by both time and distance was improperly collected. On the other hand, since Sprint did collect the 911 surcharge on the purportedly "time-only" charges, the court concurred with the Board that Sprint was not eligible for a refund of these surcharge amounts. (Order Regarding Methodology, *supra*, at p. 2:1-13; §§ 41023, 41100.) Sprint could only obtain a refund of 911 surcharge amounts if it could show that it either had not collected the 911 surcharge from its customers in the first place or that it had refunded those surcharge amounts to its customers. (§ 41100.) Sprint could show neither.

This same analysis applies to all other service suppliers, along with the analysis described in the USF charge discussion, above. The USF charge analysis regarding claims for refund by service users also applies. The only difference here is that, after May 21, 2008, all toll charges were made subject to the 911 surcharge, whether they vary by time and distance, vary only by time, or do not vary at all. (Stats. 2008, ch. 17 (Sen. Bill No. 1040).) Accordingly, only 911 surcharge amounts imposed on toll charges on bills issued to the service user prior to May 21, 2008, may be considered for refund.

I trust that this memorandum is sufficient to provide the guidance you presently need. Please let me know if you have any questions regarding the advice provided here or if you would like further assistance regarding any of these matters.

CDJ:yg

cc: Mr. Bill Kimsey (MIC:56)
Mr. Brian Ishimaru (MIC:56)
Mr. Randy Ferris (MIC:82)
Mr. Steve Smith (MIC:82)

State of California

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Memorandum

To: Lou Feletto
Administrator
Program Policy and Administration Branch (MIC:31)

Date: June 7, 2011

From: Carolee D. Johnstone
Tax Counsel III (Specialist)
Tax and Fee Programs Division (MIC:82)

Subject: ***Request for Legal Opinion – Energy Resources Surcharge and Net Energy Metering***
Assignment No. 11-060

This is in response to your February 8, 2011, request to Acting Chief Counsel Christine Bisauta for a legal opinion regarding application of the Energy Resources Surcharge (Surcharge) to net energy metering customers of electric utilities. The Board of Equalization (BOE) Special Taxes and Fees Division (STFD) has received an inquiry from the) asking for clarification of the proper application of the Surcharge to eligible customer-generators participating in a net energy metering program.

Specifically, sks how the BOE requires electric utilities to calculate the amount of surcharge due from an eligible customer-generator (customer). The question is whether the Surcharge is based on the amount of electricity supplied by the utility to the customer or on the net difference between the amount of electricity supplied by the utility and the amount of electricity generated by the customer and fed back to the electric grid.

As discussed below, the Surcharge should be applied to the total amount of electricity supplied by the utility and consumed by the customer. Whether the customer is a "net consumer" or a "net generator" of electricity does not affect how the surcharge is applied.

BACKGROUND FACTS AND LAW

Under the Public Utilities Code (PUC), "net energy metering" involves "measuring the difference between the electricity supplied through the electric grid and the electricity generated by an eligible customer-generator and fed back to the electric grid over a 12-month period . . . ." (PUC, § 2827, subd. (b)(5).) Net energy metering is accomplished by using a single meter capable of registering the flow of electricity in two directions, so that the customer is accurately billed or credited. (PUC, § 2827, subd. (c)(1).)

An "eligible customer-generator" is, in relevant part:

> [A] residential [customer], small commercial customer . . . , commercial, industrial, or agricultural customer of an electric utility, who uses a solar or a wind turbine electrical generating facility . . . with a capacity of not more than one megawatt that is located on the customer's . . . premises, and is interconnected and operates in parallel with the electric grid, and is intended primarily to offset part or all of the customer's own electrical requirements. (PUC, § 2827, subd. (b)(4).)

These customers may be net surplus generators or net consumers, and the electric utility is required to bill the customer for the electricity used during a certain period (e.g., one month or 12 months), depending on whether the customer was a net consumer or a net surplus generator during that period. (PUC, § 2827, subds. (h)(1) & (i)(3).) Where the electricity supplied by the utility exceeds the electricity generated by the customer during the same period, the customer is a net electricity consumer. (PUC, §2827, subds. (h)(2) & (i) (3).)

The Surcharge is imposed pursuant to the Energy Resources Surcharge Law (part 19 (commencing with section 40001) of division 2 of the Revenue and Taxation Code (RTC)). "A surcharge is imposed on the consumption . . . of electrical energy purchased from an electric utility," at a rate that is fixed by November of each year, to be effective the next January, by the California Energy Resources Conservation and Development Commission (Energy Commission), not to exceed three-tenths mill ($0.0003) per kilowatthour. (RTC, § 40016 [emphasis added].) "Consumption" is "the utilization or employment of electrical energy," but does not include receipt by an electric utility of electrical energy for resale, and a "consumer" is "any person receiving for consumption electrical energy furnished by an electric utility . . . ." (RTC, §§ 40008 & 40009.) Further, "[e]very person consuming electrical energy in this state purchased from an electric utility . . . is liable for the surcharge." (RTC, § 40018 [emphasis added].)

DISCUSSION

As indicated above, the Surcharge is imposed on the consumption of electricity, and every person who consumes electricity purchased from, i.e., supplied by, an electric utility is liable for the surcharge. PUC section 2827 provides that the amount of electricity consumed by customer-generators may be offset by the amount of electricity generated by these customers; the utility will bill the customer if the amount consumed exceeds the amount generated for the period and will credit or compensate the customer if the amount generated exceeds the amount consumed for the period. (See PUC, § 2827, subds. (h) & (i).) However, with the exception of certain exemptions not relevant here, no provision in the Energy Resources Surcharge Law provides for offset of the amount of electricity consumed on any basis. In other words, the fact that the customer also generates electricity does not alter the fact that the customer has consumed electricity purchased from (i.e., supplied by) an electric utility.

Furthermore, when the electric utility bills the customer at the end of each period, the amount of electricity consumed by the customer is offset by the amount of by the electricity generated by the customer and fed back to the electric grid. (PUC, § 2827, subds. (b)(5), (h), (i).) Hence, the electricity generated by the customer is a form of consideration "paid" by the customer to the

electric utility in exchange for the electricity the customer consumed, reducing the amount of money the customer would otherwise owe to the utility for the electricity it consumed. Again, the electricity generated by the customer and fed back to the grid does not reduce the amount of electricity the customer consumed.

Accordingly, the Surcharge must be applied to the total amount of electricity supplied by the utility and consumed by the customer, and whether the customer is a "net consumer" or a "net generator" does not affect how the surcharge is applied.

Please let me know if you have any questions regarding the information provided here.

CDJ/mcb

cc: Lynn Bartolo (MIC:31)
Christine Bisauta (MIC:82)
Stephen Smith (MIC:82)